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No. 516

In the Supreme Court of the United States

OCTOBER TERM, 1940

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

O. G. RICHTER

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

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The Solicitor General, on behalf of Guy T. Helvering, Commissioner of Internal Revenue, prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Third Circuit entered in the above cause on July 17, 1940.

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 16–17) is not officially reported. The opinion of the United States Circuit Court of Appeals for the Third Circuit (R. 28–30) is not yet officially reported.

JURISDICTION

The judgment of the United States Circuit Court of Appeals was entered July 17, 1940 (R. 30). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

The taxpayer transferred securities to a third party in trust to pay the income to his wife. At the end of five years, or earlier if the beneficiary consented, the securities were to be transferred back to the taxpayer. The Board of Tax Appeals held that the grantor was not taxable with respect to the income from the trust. Two questions are presented:

1. Whether, by invoking the general gross income provisions of Section 22, the Commissioner had so changed the theory of the Government's case on appeal as to preclude the Circuit Court of Appeals from considering the issue.

2. Whether, on the merits, the trust income was taxable as income of the grantor under Section 22.

STATUTE AND REGULATIONS INVOLVED

Revenue Act of 1934, c. 277, 48 Stat. 680:

> SEC. 22. GROSS INCOME.
>
> (a) *General Definition.*—"Gross income" includes gains, profits, and income derived from salaries, wages, or compensation for personal service, of whatever kind and in

> whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *
>
> (U. S. C., Title 26, Sec. 22.)

The applicable provisions of Article 166–1 of Regulations 86, as amended, appear in the Appendix, *infra*.

STATEMENT

The facts were stipulated before the Board of Tax Appeals (R. 8–16). The Board adopted the stipulated facts as its findings of fact (R. 16), which may be summarized as follows:

By a trust instrument dated December 29, 1930, the taxpayer placed a group of securities in trust with the Union Trust Company of Pittsburgh, to pay, during the duration of the trust, the net income of the trust to Nannie C. Richter, the taxpayer's wife, in such installments as she might request. Provision for termination of the trust was as follows (R. 11–12):

> The Donor reserves the right to terminate this trust at any time during the continuance hereof with the consent of the beneficiary, and not otherwise, by giving thirty days notice in writing of his intention so to do, accompanied by the written consent of the

beneficiary, served upon the Donor, which thirty day period of notice may be waived by the Trustee, and, upon the exercise of this power of revocation, this trust shall and the moneys, securities, and properties then held under the terms hereof, shall be transferred, assigned and delivered to the Donor, or his nominee or nominees, and the receipt of the said Donor, or his nominee or nominees, shall be full and sufficient discharge of the Trustee with respect thereto.

In the event that this trust is not sooner terminated as above provided, it shall end on January 3, 1936, and the original corpus and additions, if any made thereto subsequently by the Donor, shall be paid, assigned, transferred, and delivered to the Donor as hereinbefore provided; and, in the event of the death of the Donor or the cestui que trust during the continuance of this trust, such decease shall operate as a revocation and the original corpus and any additions, if any made thereto subsequently by the Donor, shall be transferred, assigned, and paid over to the Donor or his legal representatives, discharged of the trust herein.

By instrument dated June 3, 1932 (R. 15–16), the taxpayer extended the term of the trust to January 3, 1938, provided that the trust was not sooner terminated by act of the taxpayer-settlor and consent of the beneficiary, or by death of the settlor or beneficiary. The taxpayer did not at any time have any agreement with his wife that she would join with him upon his request for a

termination of the trust prior to the time specified for its termination. Taxpayer at no time asked his wife to join in an agreement for termination, and she at no time offered to join with him in any agreement for termination. Taxpayer's wife died on November 26, 1935 (R. 9, 10).

The trust was in effect throughout the year 1934, and the trustee paid the entire net income of the trust for that year to taxpayer's wife (R. 9, 10). In determining the income tax liability of the taxpayer for the calendar year 1934, the Commissioner attributed the income of the trust to the taxpayer and determined a deficiency accordingly.

The taxpayer sought review in the Board of Tax Appeals, where the Commissioner undertook to defend his determination on two grounds: (1) that the income was taxable to the grantor under Section 166 of the Revenue Act of 1934; and (2) that the grantor retained such substantial incidents of ownership in the corpus as to render him taxable upon the income therefrom under Article 166–1 of Regulations 86, as amended.[1] The Board held the grantor not taxable.

Upon appeal to the Circuit Court of Appeals, the Commissioner again urged not only that the grantor was taxable under Section 166 of the 1934 Act, but

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[1] This second theory appears as Point III of the brief filed by the Commissioner with the Board of Tax Appeals.

also that the income was attributable to him under Article 166–1 of Regulations 86, as amended (R. 20, 23). However, subsequently, as a result of this Court's supervening decisions in *Helvering* v. *Clifford*, 309 U. S. 331, and *Helvering* v. *Wood*, 309 U. S. 344, the Commissioner waived reliance upon Section 166, but sought to have the income taxed under Section 22 (a), which contained the statutory provisions supporting Article 166–1 of Regulations 86, previously relied upon. The Circuit Court of Appeals refused to consider Section 22 (a) on the theory that it was being raised for the first time on appeal, and affirmed the decision of the Board.

SPECIFICATION OF ERRORS TO BE URGED

The Circuit Court of Appeals erred:

1. In holding and deciding that the income derived from the Nannie C. Richter Trust during the calendar year 1934 was not taxable to the grantor, O. G. Richter.

2. In failing to hold and decide that the income of the Nannie C. Richter Trust for the calendar year 1934 was taxable to the grantor as his income in the year 1934.

3. In failing to hold that the trust income was taxable to the grantor under Article 166–1 of Treasury Regulations 86, as amended.

4. In failing to hold that the foregoing provisions of Article 166–1 are supported by Section 22 (a) of the Revenue Act of 1934.

5. In holding that the applicability of Section 22 (a), *supra*, involved a new issue which could not be presented on appeal.

6. In failing to hold that the taxability of the trust income to the grantor was, in a broad sense, the issue before the Board of Tax Appeals.

7. In failing to reverse the decision of the Board of Tax Appeals.

REASONS FOR GRANTING THE WRIT

1. In denying the Government the right to rely upon the general provisions of Section 22 (a) merely because they had not been specifically mentioned before the Board, the decision of the court below is in conflict with *Helvering* v. *Hormel,* 111 F. (2d) 1 (C. C. A. 8th), certiorari granted, October 14, 1940, No. 257, present Term.

2. This case presents an important question as to the scope of review in the circuit courts of appeals which is in need of clarification.

The Government relied upon the amended provisions of Article 166–1 of Regulations 86 (see Appendix, p. 10, *infra*) in the Board of Tax Appeals. Upon appeal, it continued to rely upon the same provisions, and brought the case into sharper focus by invoking Section 22 (a) of the Revenue Act of 1934 which afforded statutory support for those provisions. There was no change in theory upon which taxability was predicated. The theory of taxability was the same whether couched in terms of Article 166–1 or in terms of Section 22

(a), as construed in *Helvering* v. *Clifford,* 309 U. S. 331.[2] The Government's position on appeal involved no additional elements to be considered, since the same criteria of taxability set forth in the *Clifford* decision were likewise contained in Article 166–1. There was simply a shift of emphasis from the regulations to the statute, the theory of taxability remaining unchanged.

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[2] The Court in the *Clifford* case put aside the consideration of Article 166–1, since the amended provisions had been promulgated after the tax year in question. 309 U. S. at 334, n. 1. Although the tax year here likewise preceded the amendment, the Government nevertheless did in fact rely upon the amended regulations in the Board, so that, at least for the purpose of scope of review, it cannot be said that the Government changed the theory of the tax upon appeal when it simply invoked Section 22 (a), which was the statutory basis for the amended regulations.

Moreover, even though the Court in the *Clifford* case found it unnecessary to rest its decision upon the amended regulations, they were nevertheless applicable, unless invalid, to the tax year in question. The regulations involved were Regulations 86, which governed income-tax liability under the Revenue Act of 1934, *i. e.*, income-tax liability for the years 1934 and 1935. (The year 1936 and later years were governed by the Revenue Act of 1936 and later Acts.) The 1936 amendment to Regulations 86, here involved, would have been entirely without meaning unless it were to apply to the years ruled by the 1934 Act (*i. e.*, 1934 and 1935). And the scheme of the revenue acts contemplates that changes in regulations are to relate to all tax years governed by the regulations unless the Secretary of the Treasury or the Commissioner affirmatively provide that the change shall have only prospective application. Section 1108 (a) of the Revenue Act of 1926 (c. 27, 44 Stat. 9), as amended by Section 506 of the Revenue Act of 1934, specifically provides

It would seem that the court below unduly limited its power of review. And since scope of review in somewhat similar situations frequently confronts the circuit courts of appeals, it is a matter of considerable importance to obtain clarification of their power in such circumstances.

CONCLUSION

Therefore, it is respectfully submitted that this petition for a writ of certiorari should be granted.

FRANCIS BIDDLE,
Solicitor General.

OCTOBER 1940.

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that "The Secretary, or the Commissioner with the approval of the Secretary, may prescribe the extent, if any, to which any ruling, regulation, or Treasury Decision, relating to the internal revenue laws, shall be applied without retroactive effect." See *Morrissey* v. *Commissioner*, 296 U. S. 344; but cf. *Helvering* v. *Reynolds Tobacco Co.*, 306 U. S. 110. Unlike the amended regulations in the *Reynolds* case, however, the amended regulations here created no new rule of liability: the amended regulations here simply sharpened the legal theory upon which income theretofore attributed to the grantor was to be included in his gross income.

APPENDIX

Treasury Regulations 86, promulgated under the Revenue Act of 1934:

> ART. 166–1 [as amended by T. D. 4629, XV–1 Cum. Bull. 140, 141 (1936), and T. D. 4759, 1937–2 Cum. Bull. 117, 118]. *Trusts, with respect to the corpus of which, the grantor is regarded as remaining in substance the owner.*—(a) If the grantor of a trust is regarded, within the meaning of the Act, as remaining in substance the owner of the corpus thereof, the income therefrom is not taxable in accordance with the provisions of sections 161, 162, and 163 but remains attributable and taxable to the grantor. This article deals with the taxation of such income. As used in this article, the term "corpus" means any part or the whole of the property, real or personal, constituting the subject matter of the trust.
>
> (b) * * *
>
> But the provisions of section 166 are not to be regarded as excluding from taxation to the grantor the income of other trusts, not specified therein, in which the grantor is, for the purposes of the Act, similarly regarded as remaining in substance the owner of the corpus. The grantor is regarded as in substance the owner of the corpus, if, in view of the essential nature and purpose of the trust, it is apparent that the grantor has failed to part permanently and definitively with the substantial incidents of ownership in the corpus.

In determining whether the grantor is in substance the owner of the corpus, the Act has its own standard, which is a substantial one, dependent neither on the niceties of the particular conveyancing device used, nor on the technical description which the law of property gives to the estate or interest transferred to the trustees or beneficiaries of the trust. In that determination, among the material factors are: the fact that the corpus is to be returned to the grantor after a specific term; the fact that the corpus is or may be administered in the interest of the grantor; the fact that the anticipated income is being appropriated in advance for the customary expenditures of the grantor or those which he would ordinarily and naturally make; and any other circumstances bearing on the impermanence and indefiniteness with which the grantor has parted with the substantial incidents of ownership in the corpus.

Thus the grantor is regarded as being in substance the owner of the corpus if, in any case, the trust amounts to no more than an arrangement whereby the grantor, in the ordering of his affairs, finds it expedient to entrust for a period the title to, and custody or management of, certain of his property to a trustee, the income from such property to be used by the trustee during such period to make those expenditures which the grantor would customarily or ordinarily or naturally make and to which the grantor chooses to commit himself in advance, while the corpus is to be held intact, for return in due course to the grantor. In such a case, it is immaterial that, at the time of the creation of the trust, an irrevocable disposition or consummated gift was made of those property rights

which consist of the right to the expected future income of the corpus for the specified period. On the other hand, if the grantor, incident to a definitive and permanent disposition of certain of his property, creates the trust in order to conserve the property, not for himself but for the donees, who will ultimately enjoy it, the provisions of sections 161, 162, and 163 are applicable.

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